

Research Update:

Eutelsat Communications Raised To 'BBB-' On Solid Operating Performance And Improved Leverage; Outlook Stable

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Overview

- France-based satellite operator, Eutelsat Communications, has posted a solid operating performance and we believe that risks linked to the group's very high capacity utilization are declining.
- We are raising the group's ratings to 'BBB-/A-3' from 'BB+/B'.
- All corporate credit ratings were removed from CreditWatch where they had been placed with positive implications on June 30, 2009.
- The stable outlook reflects our view that the group's leverage will improve and that its revenue and earnings growth will continue over the next few years.

Rating Action

On Nov. 23, 2009, Standard & Poor's Ratings Services:

- Raised its long-term corporate credit ratings to 'BBB-' from 'BB+' on Eutelsat Communications S.A. (Eutelsat) and related entity Eutelsat S.A. The outlook is stable.
- Raised Eutelsat's and Eutelsat S.A.'s short-term corporate credit ratings to 'A-3' from 'B'.
- Affirmed its 'BBB-' debt rating on Eutelsat S.A.'s €1.3 billion bank loan due 2011, and withdrew its '2' recovery rating on the loan, as a result of the upgrade of the long-term corporate credit rating to investment grade.
- Removed all corporate credit ratings from CreditWatch where they had been placed on June 30, 2009, with positive implications.

Rationale

The rating actions mainly reflect Eutelsat Communications' solid operating performance in fiscal 2009 and in the first quarter of fiscal 2010, as well as our expectations that the group's revenues and earnings should continue to grow in the medium term. Also, we believe that the upcoming W7 satellite launch, together with satellite launches made since the end of 2008, have reduced the risks linked to the group's high capacity utilization rate. Finally, the rating upgrade also reflects the group's prudent financial policy over the past few years, especially regarding acquisitions and dividend distribution, and expectations that this will continue in the future, resulting in adjusted leverage of less than 3.5x over the medium term.

Eutelsat Communications' solid operating performance over the past few years

has resulted in a steady reduction in leverage since its leveraged buyout in 2005. The group's adjusted net debt-to-EBITDA ratio fell to 3.2x in fiscal 2009 (ended June 30, 2009), from 3.8x in fiscal 2006. Eutelsat Communications' revenue increased by 7.2% in fiscal 2009, and accelerated to 11.6% in the first quarter of fiscal 2010, owing to sustained demand for satellite services and the entry into commercial service of additional satellite capacity.

Eutelsat Communications has launched three satellites and repositioned another three since the beginning of 2009, allowing the group to reduce its utilization rates to 88.8% at the end of June 2009, from the very high 97% recorded at Dec. 31, 2008. While high utilization rates generally result in higher profitability, they may also limit the ability to meet additional demand and therefore to strengthen revenues and earnings. They may also limit the ability to provide sufficient backup capacity in the event of one or multiple satellite in-orbit failures. Eutelsat Communications expects to launch another five satellites before the end of 2011 to replace existing satellites and to be in a position to adequately absorb current demand for its services.

Upcoming satellite launches are, however, expected to result in weak free cash flows and negative discretionary cash flows over the next two years, as the group anticipates that capital expenditures will peak in fiscal 2010 and 2011. We believe, however, that this could be mitigated by good earnings visibility and the additional capacity that the upcoming satellite launches will provide.

The ratings on Eutelsat Communications continue to reflect its position as one of Europe's leading providers of satellite capacity for the video segment; its strong asset infrastructure; and a solid contracted revenue backlog of €3.9 billion at June 30, 2009, which provides good sales and cash flow visibility along with strong profitability. The group has a relatively complex capital structure, however, and has to commit to large capital expenditures in its business, which entails significant operational risks inherent to the launch and operation of satellites.

Liquidity

Eutelsat Communications had sufficient liquidity at June 30, 2009, to support its business needs. The group's liquidity, however, mostly hinges on access to committed credit lines to fund part of its capital expenditures or dividend payments, as cash balances are generally modest. Financial flexibility mostly revolves around operating company Eutelsat S.A.'s (BBB-/Stable/A-3) €650 million committed revolving credit facility, which matures in November 2011, and under which about €450 million was available as of June 30, 2009.

Cash balances stood at €144 million at the same date, while short-term debt was about €14 million, essentially composed of accrued interests.

The group's reliance on the €650 million revolver is important, as free cash flow is likely to remain modest and approximately cover dividend payments over the next two years. The group paid dividends of about €145 million in fiscal

2009, and we believe dividend growth should remain in line with earnings over the medium term. The group does not, however, have any significant debt maturities before November 2011, when Eutelsat S.A.'s €1.3 billion syndicated loan and revolving facility will mature. Eutelsat Communications' €1.6 billion term loan will mature in June 2013.

Dividends upstreamed from Eutelsat S.A. to Eutelsat Communications are the only source of funds for paying interest and external dividends at the holding company level, and are supported by a €300 million revolving credit facility for any shortfalls. Eutelsat Communications' interest payments are mostly fixed rate, after swap effects. In addition, we believe that Eutelsat Communications lends to Eutelsat S.A. most of its excess cash once its own financial interests and external dividends have been paid, in order to optimize group funding costs. We estimate the amount of these financial receivables to be potentially significant on an annual basis, and that the group may access them if needed. The €300 million revolver, along with over €350 million of distributable reserves, provides adequate headroom for underperformance at the operating level or for potential technical accounting adjustments, either of which could affect the net distributable result at the Eutelsat S.A. level. A major technical failure at one or more of the group's satellites could result in large asset impairments and impact Eutelsat S.A.'s net income, although we would reasonably expect related insurance proceeds to broadly offset this shortly after the occurrence of such incidents.

In addition, dividend payments made to external shareholders by Eutelsat Communications may contribute to limiting financial flexibility in the medium term, although we expect the group to partially offset this by continuing to maintain sufficient cash balances or equivalent at Eutelsat Communications.

Outlook

The stable outlook reflects our view that the group's improving leverage, and anticipations of continued revenue and earnings growth over the next few years should enable the group to have credit measures commensurate with investment grade ratings in the medium term. In order to maintain the current ratings, we would expect the group to post adjusted net debt to EBITDA of less than 3.5x. The outlook also reflects our expectations that the group's financial policy will continue to be prudent over the next few years, particularly in terms of acquisitions and dividend distribution.

We could consider a downgrade if the group were to post significant operating underperformance, or if it were to suffer material satellite failures over the next few years. Downside rating risk could also materialize if the group's financial policy were to become more aggressive, in particular through major acquisitions and/or excessive shareholder distributions resulting in permanently higher-than-expected adjusted leverage.

Rating upside may, in the future, stem from continued solid operating performance, coupled with material improvements in free cash and discretionary

cash flow generation, as well as expectations of a permanent improvement in credit measures. Continuation of a prudent financial policy would also be an important factor.

Related Research

Criteria Methodology: Business Risk/Financial Risk Matrix Expanded, May 27, 2009

Ratings List

Upgraded; CreditWatch/Outlook Action

	To	From
Eutelsat Communications S.A.		
Eutelsat S.A.		
Corporate Credit Rating	BBB-/Stable/A-3	BB+/Watch Pos/B

Ratings Affirmed; Recovery Rating Withdrawn

Eutelsat S.A.		
Senior Unsecured	BBB-	
Recovery Rating	NR	2

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